

UNITED NATIONS GENERAL ASSEMBLY



Distr.
GENERAL
A/CN.9/397
29 April 1994

ORIGINAL: ENGLISH

UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW

Twenty-seventh session

New York, 31 May - 17 June 1994

POSSIBLE FUTURE WORK

Legal Aspects of Receivables Financing

Report of the Secretary-General

Contents

	<u>Paragraphs</u>	<u>Page</u>
INTRODUCTION	1-2	2
I. SCOPE OF WORK	3-19	2
A. Assignment of receivables	3-5	2
B. Assignment by way of sale and by way of security	6-9	3
C. Non-notification assignment	10	5
D. Factoring	11-12	5
E. Forfaiting	13	6
F. Securitization	14-15	6
G. Project finance	16	7
H. Commercial or consumer receivables	17	7
I. International or domestic receivables	18-19	7
II. POSSIBLE ISSUES	20-51	8
A. Assignability of receivables	20-25	8
1. No-assignment clauses	21-23	8
2. Bulk assignments	24-25	9
B. Form requirements	26-27	9
C. Effects of assignment between the assignor and the assignee	28	10
D. Effects of assignment towards the debtor	29-35	10
E. Effects of assignment towards third parties; priorities	36-42	12
F. Registration	43-51	14
CONCLUSION	52-56	17

INTRODUCTION

1. The Commission at its twenty-sixth session in 1993 considered a note by the Secretariat containing a brief discussion of certain legal problems in the area of assignment of claims and of past and current work on assignment and related topics.¹ After considering that note, the Commission requested the Secretariat to prepare, in cooperation with UNIDROIT and other international organizations, a study on the feasibility of unification work in the field of assignment of claims, so as to permit the Commission to decide at its twenty-seventh session whether it should undertake work in this area of law.² The present report has been prepared pursuant to that request. The report focuses on assignment of receivables as the legal technique used in the context of receivables financing.

2. With a view to determining the feasibility of any future work on receivables financing, the first part of the report discusses the possible scope of such work, and for the purposes of the discussion defines the concepts used in the report; in the second part, some problems arising in assignment of receivables are discussed along with possible solutions that could be adopted in any future uniform rules, whether in a convention or in a model law. In implementing its mandate to prepare this report in cooperation with UNIDROIT and other international organizations, the Secretariat made a preliminary draft of the report available to UNIDROIT, the Hague Conference on Private International Law and the European Bank for Reconstruction and Development (EBRD) for their comments. In addition, the Secretariat will orally introduce this report to the Governing Council of UNIDROIT at its upcoming meeting (Rome, 9 to 14 May 1994).

I. SCOPE OF WORK

A. Assignment of receivables

3. "Receivables financing" is a term used in practice to describe a wide range of transactions in which finance is raised on the basis of receivables. Receivables financing may be linked to complex transactions, such as joint ventures, other contractual arrangements or the issuance of securities.³ In an assignment of receivables, a party ("assignor") transfers to another party ("assignee") payment claims that the assignor has against a third party ("debtor") under a separate transaction for goods sold or leased, facilities made available or services rendered ("the original transaction"). The assignment is given in fulfilment of a sales or credit transaction in which the assignor is the debtor and the assignee is the creditor ("the underlying transaction"). The term "receivables", although there does not seem to be a generally accepted definition, is widely used as a generic description of payment claims. Receivables financing may involve assignments by way of sale or by way of security (see paragraphs 6-9), non-notification assignments (see paragraph 10), factoring (see paragraphs 11-12), forfaiting (see paragraph 13), or even more sophisticated techniques such as particular forms of securitization and project finance (see paragraphs 14-16).

¹ A/CN.9/378/Add.3.

² Report of the United Nations Commission on International Trade Law on the work of its twenty-sixth session (1993), Official Records of the General Assembly, Forty-eighth Session, Supplement No. 17 (A/48/17), para. 301.

³ Fidelis Oditah, Legal aspects of receivables financing (Sweet & Maxwell 1991), p. 19.

4. It would appear that some unification work in the field of receivables financing might be considered both desirable and feasible. The differences existing between legal systems on assignment of receivables, and the fact that States generally require compliance with their own requirements and formalities for an assignment to be valid and effective towards the debtor and third parties, may result in one and the same assignment being valid in the State where it was concluded but unenforceable against the debtor in another State. In addition, the uncertainty of law resulting from the lack of adequate modern rules on assignment of receivables may render assignment impractical in a cross-border context. As a result parties may often be forced to forego receivables financing in international trade and to revert to other, potentially more expensive means of financing, such as overdraft facilities, letters of credit or export guarantees, or to secure receivables through bank guarantees or letters of credit, or to accept that receivables are assigned at a value substantially less than their face value, due to the high risk that the assignee may not be able to collect part or all of their value.

5. Recent unification work in a part of this area of law may be seen as an indication that unification in the area of receivables financing may be considered feasible. The UNIDROIT Conventions on International Factoring and on International Financial Leasing (Ottawa, 1988) have been ratified by two States and require one more ratification or accession in order to enter into force. In addition, a number of countries in which the EBRD operates are about to enact or consider enacting legislation based on the Model Law on Secured Transactions prepared by the EBRD.

B. Assignment by way of sale and by way of security

6. Receivables may either be sold or used as security, or, stated in commercial terms, they may be assigned in order to generate income (when they are sold) or to facilitate access to credit (when they are used as security). Assignment of receivables by way of sale may be defined as the transaction whereby the assignee acquires full property rights on the assigned receivables, advancing all or part of their value to the assignor. Assignment by way of sale may be with or without recourse, that is, it may or may not provide for the assignor to guarantee the assignee against default by the debtors. Such assignment is also known in practice as "invoice discounting" or "block discounting" (see paragraph 8). In certain circumstances, it is also referred to as "factoring" (see paragraphs 9-10). Assignment of receivables by way of security is the transaction whereby the assignee acquires limited property rights in the assigned receivables, in the sense that the assignee is entitled to collect them only in the event that the assignor defaults in the performance of its obligations towards the assignee under the underlying credit transaction. It may be noted that, in some jurisdictions, the assignee in an assignment by way of security acquires title to the receivables, and it is only the underlying transaction that may limit its powers if it is a credit transaction. While to a large extent the same issues arise in both kinds of assignment, there are some differences. For example, in case of default of the assignor in the performance of the underlying transaction, if an assignment by way of sale is involved, the assignee can retain any surplus from the assigned receivables that it collects, while in assignment by way of security any surplus is to be returned to the assignor. In addition, in case of assignment by way of security, if the assignee collects the assigned receivables from the debtor without the assignor having defaulted in the performance of the underlying transaction, it may be liable to the assignor for breach of contract.

7. There are several possible approaches as to the manner in which assignment of receivables could be addressed in the context of uniform rules. One possibility, based on an approach followed in some jurisdictions, would be to address assignment in general terms, and to leave specific issues of assignment by way of sale to the national law on sales, and specific issues of

assignment by way of security to the national law on credit transactions. The main disadvantage of such an approach would be that, to a large extent, it would fail to produce uniform results. Another approach, followed in other jurisdictions, would be to cover assignment as a predominantly sales transaction. While such an approach would not preclude States from applying the uniform rules to assignment by way of security as well, it would fail to regulate an important part of receivables financing that could benefit from any uniform rules. In addition, it would fail to recognize the fact that, to a large extent, the issues raised in assignment by way of sale and by way of security are identical. Moreover, it would have the disadvantage of resulting in a duality of regimes. Yet another approach, followed in other jurisdictions and recommended here, would be to address both kinds of assignment in a single set of rules. Such an approach would have the advantage of recognizing the financing purpose of both kinds of assignment. Sales of receivables that are not for financing purposes, e.g., sales for collection only, sales in which the assignee is to perform the obligations of the assignor under the original transaction, sales of single receivables in payment of preexisting debts and sales as part of a sale of a business, would presumably have to be excluded. While most issues could be addressed by common rules applicable to both kinds of assignment, other issues would have to be dealt with differently, e.g., the issue of default of the assignor.

8. In some jurisdictions, assignment by way of security is referred to as a secured transaction, namely, a transaction creating a security right in receivables in the sense of a limited property right of the assignee to collect the receivables in case the assignor defaults in the performance of the underlying transaction. In those jurisdictions, even assignments by way of sale are viewed as secured transactions, provided that they are made for financing purposes. At the same time, in such jurisdictions, secured transactions are regulated in a comprehensive way in the sense that a single set of rules governs secured transactions in personal property, including goods, mobile equipment, inventory, receivables and general intangibles. It may be noted that such a comprehensive approach will be considered by the UNIDROIT Secretariat which has been authorized by the Governing Council at its 72nd session in June 1993 to prepare a study on the feasibility and desirability of drawing up a model law on secured transactions.⁴ In the preparation of that study and the eventual elaboration of any draft rules close cooperation between the Commission and UNIDROIT seems desirable (see also below, para. 55).

9. If the UNIDROIT study were to establish the feasibility of such a comprehensive approach, the relationship between such work and the suggested project on receivables financing would have to be decided upon in concrete terms, in particular whether any draft statutory provisions on receivables financing should eventually be incorporated into a considerably more comprehensive model law; at least, there should be means to prevent substantive inconsistencies between texts on transactions with common characteristics. It may be added that UNIDROIT itself would face the same situation in a more acute manner, in view of the fact that it currently follows also the sectoral approach by preparing a draft convention on certain aspects of security interests in mobile equipment, based on the understanding that a narrowly defined scope of work is an indispensable condition of the feasibility of such work.⁵

⁴ UNIDROIT 1994, C.D. (73)8.

⁵ UNIDROIT 1992, Study LXXII - Doc. 5, para. 6.

C. Non-notification assignment

10. "Non-notification assignment" refers to a type of assignment in which the debtor is not notified of the assignment. A major reason for using a non-notification assignment is that assignment may be viewed as indicating financial or managerial weakness of the assignor. The debtor may be notified only in exceptional circumstances, such as in the case of insolvency of the assignor, where the assignee may need to enforce the receivables against the debtor. Non-notification assignment is inherently more risky for the assignee, since the debtor can pay the assignor and be discharged. In addition, depending on whether priority among several assignees is based on notification of the debtor or registration of the assignment, a subsequent assignee notifying the debtor first or registering the assignment first will have priority. Examples of non-notification assignment include "block discounting" and "invoice discounting". "Block discounting" involves a non-notification sale of receivables in which the assignee retains, in addition to a security in the form of part of the face value of the receivables, a discount calculated by the average period during which it will be out of its money. The assignee usually undertakes to collect the receivables as an agent of the assignor and to guarantee payment by the debtors. "Invoice discounting" involves a non-notification sale of receivables in which the assignor continues to be responsible for collections as agent of the assignee, the undisclosed principal.⁶

D. Factoring

11. Factoring is often understood in practice as the sale of receivables for financing and other purposes. However, the UNIDROIT Convention on International Factoring ("the UNIDROIT Factoring Convention") covers both assignments by way of sale and by way of security. For the purposes of the Convention, factoring means "a contract concluded between one party (the supplier) and another party (the factor) pursuant to which: (a) the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and its customers (debtors) other than those for the sale of goods bought primarily for their personal, family or household use; (b) the factor is to perform at least two of the following functions: finance for the supplier, including loans and advance payments; maintenance of accounts (ledgering) relating to receivables; collection of receivables; protection against default in payment by the debtors; (c) notice of the assignment of the receivables is to be given to debtors." (art. 1). The Convention further specifies that "goods" includes services (art. 1(2)) and that the Convention applies when the receivables arise from international sales of goods (the supplier and the debtor have their places of business in different countries) and the factor is situated in a third country or when both the contract of the sale of goods and the factoring contract are governed by the law of a contracting State (art. 2).

12. Thus the Convention addresses a considerable number but not all kinds of factoring, and it leaves a number of issues arising in the area of factoring to the applicable national law (the title initially used for the Convention, i.e., "draft Convention on Certain Aspects of International Factoring", clearly indicated that it was not intended to be comprehensive). In particular, the Convention does not cover factoring, if only financing, or just one additional service from the ones enumerated in article 1 of the Convention, is offered. The Convention does not cover assignment of domestic receivables or of receivables arising from leases or from transactions on the basis of which equipment or facilities are made available. Moreover, the Convention does not apply to non-notification assignment, such as block discounting or invoice discounting. At the same time,

⁶ Roy M. Goode, Commercial law (Penguin Books, 1982), p. 856.

the Convention does not cover certain issues arising in assignment of receivables, especially effects of assignment towards third parties.

E. Forfaiting

13. Forfaiting may be described as the sale of documentary receivables, that is receivables incorporated in negotiable instruments, such as bills of exchange, promissory notes, or in letters of credit and bank guarantees. However, the term "forfaiting" may be used to indicate the sale of non-documentary receivables that often may be backed by a bank guarantee or a letter of credit. Any unification work on forfaiting of documentary receivables might not be desirable in view of the fact that the assignment of such documentary receivables is already regulated by uniform statutory rules (e.g., the Geneva Uniform Laws on Bills of Exchange, Promissory Notes and Cheques), or uniform rules at the contractual level (e.g., assignment of proceeds of letters of credit under the ICC Uniform Customs and Practice for Documentary Credits and assignment of proceeds of bank guarantees subject to the ICC Uniform Rules on Demand Guarantees), or is the subject of other ongoing unification work (e.g., the UNCITRAL draft Convention on Independent Guarantees and Stand-by Letters of Credit). In addition, it should be noted that the issues arising in assignment of receivables would have to be addressed differently if documentary receivables were involved. For example, in the assignment of documentary receivables only defences based on the document incorporating the receivables could be raised by the debtor against the assignee, and priority among several assignees would have to be based on possession of the document in due course. However, future unification work could cover forfaiting of non-documentary receivables.

F. Securitization

14. Possible future work of unification could extend to a wide range of transactions described by the term "securitization", which may involve, assignment of receivables, not from a trader to a financing institution, but from one financing institution to another. Securitization may serve a number of different purposes and encompass a wide range of assets while there does not seem to be a uniform definition or practice of securitization, it may be described as the transformation of non-marketed assets, such as home mortgage loans, into marketable assets, such as securities. A basic, general structure of securitization that may involve the assignment of trade receivables from one financing institution to another for refinancing purposes may be described as follows: in a first step, the company or companies that created a discrete pool of financial assets ("the originator") may transfer them to another company, in return for capital stock or cash. In a second step, the initial transferee further transfers the assets to an investment fund, in return for cash and securities, i.e., equity or debt instruments of the type that the fund issues and sells to investors ("asset backed securities"). The initial transferee may take all the risk of loss on the assets and may have no recourse against the originator. Holders of securities issued by the investment fund may be entitled to a monthly distribution of interest at a stated rate.

15. Securitization is a relatively new financing technique growing internationally, which may serve a number of purposes, such as improvement of accounting status (e.g., replacement of non-cash assets on balance sheets by cash, improvement of return-on-assets and capital-to-assets calculations, which may improve the originator's standing towards its creditors), capital raising (higher credit rating for the securities than the originator itself possesses and lower financing costs) and regulatory compliance (e.g., compliance with lending limits and capital adequacy requirements).

G. Project finance

16. Work in the area of receivables financing could be relevant to project finance in which future revenues of an income-generating project are used to secure financing. Project finance may involve a sophisticated structure of a number of transactions, including assignment of receivables. It is a financing technique often used in projects related to the exploitation of natural resources, or projects related to the improvement of infrastructure, such as construction of power plants, bridges, highways and similar facilities. Project finance of this type appears to be increasingly of interest, in particular for developing countries and countries whose economies are in transition.

H. Commercial or consumer receivables

17. Future work could be restricted to commercial transactions, or it could encompass consumer transactions as well. One reason for not covering consumer transactions is that consumer law usually involves social policy matters that States tend to wish to decide for themselves, and is, therefore, not easily unified. Another reason might be that, at least at the present time, the volume of consumer transactions taking place at an international level might be too small to justify their consideration in an international context. It might, therefore, be preferable to limit the scope of any future work to commercial receivables only. On the other hand, the notion of "commercial" or "trade" receivables might raise some difficulties since, in some jurisdictions, no discrete body of commercial law exists. In other jurisdictions, the notion of "commercial" is defined on the basis of the nature of the transaction, or on the basis of the capacity of the parties as "merchants". It may be noted that the UNIDROIT Factoring Convention, like the United Nations Sales Convention, focuses on commercial transactions by excluding those transactions that are not "for personal, family or household" purposes.

I. International or domestic receivables

18. Another question of relevance to the scope of work is whether any possible future uniform law should apply to receivables arising only from international or also from domestic transactions. The criterion utilized in modern conventions, such as the United Nations Sales Convention and the UNIDROIT Factoring Convention, as the sole criterion for determining the internationality of a transaction is the place of business of the parties involved. Such an approach is deemed to be preferable from the standpoint of simplicity and maximization of the scope of work.⁷ In favour of addressing both international and domestic receivables, it could be maintained that the same need for legal certainty exists both in domestic and international trade. Moreover, a duality of regimes, a national one for domestic receivables and a uniform one for international receivables, might create obstacles to trade by adding to the existing diversity of applicable legal regimes. On the other hand, limiting the scope of any possible future work to international receivables would be in line with the purpose of facilitating international trade. Moreover, States might be reluctant to accept alterations of their national laws on assignment purely in a domestic context. In addition, a set of rules applicable only to international transactions might have a unifying effect even with regard to domestic transactions, since it would be open to individual States to apply these rules to domestic transactions as well. It might, therefore, be more appropriate to limit the scope of work to international receivables only.

19. However, a further limitation of the scope of future work to international assignments of international receivables only (i.e., when the assignor and the debtor have their places of business in different countries) would be unwarranted. Such a limitation could result in excluding the bulk

⁷ Roy M. Goode, Reflections on the harmonization of law, Uniform Law Review, 1991, I, p. 64.

of the assignments since assignments are usually domestic. In addition, the crucial problem of the possible unenforceability of international receivables arises irrespective of whether the assignment is domestic or international. Moreover, if future work were limited to international assignments only, there would be two legal regimes governing assignment, one applying to domestic assignments and another applying to international assignments. It may be noted that the UNIDROIT Factoring Convention applies to both domestic and international factoring of international receivables.

II. POSSIBLE ISSUES

A. Assignability of receivables

20. Generally speaking, all receivables are assignable, unless their assignment is prohibited by agreement, by statute, or due to public policy considerations. Statutory prohibitions of assignment of receivables, such as prohibitions against assignment of wages, will not be considered in this report; it would not be feasible or appropriate to attempt to prepare uniform rules covering all kinds of statutory prohibitions. However, prohibitions by agreement and prohibitions due to public policy will be touched upon below, in view of their practical importance (see paragraphs 21-25).

1. No-assignment clauses

21. Parties often include in their contracts a clause precluding the creditor from assigning the rights arising therefrom. Legal systems differ as to the extent to which such clauses are upheld. Assignments concluded in violation of such clauses are in some jurisdictions valid in general, in other jurisdictions valid only as between the original creditor/assignor and the assignee, and generally invalid in yet other jurisdictions.

22. One approach that might be considered for a uniform text would be to treat an assignment concluded in violation of a no-assignment clause as valid only if certain requirements are met. Such an approach might have the advantage of protecting the debtor from a number of adverse effects that might arise from a change in the identity of the creditor, including: the burden of having to keep track of one or more assignments; the risk that the debtor might overlook a notice of assignment and have to pay a second time; and the risk that the debtor might not be able to set up against the assignee all defences, regardless of whether they arose before or after the notice of assignment. One possible requirement would be that, within a certain time period, the debtor does not object to, or consents to, an assignment concluded in violation of a no-assignment clause. However, it might be difficult to establish a method to calculate the time period. Moreover, adopting such a requirement would enable the debtor to decide which of several conflicting assignees would have priority merely by consenting to one assignment and objecting to another. Such a result would not be in line with the purpose of the no-assignment clause, which is to protect the interests of the debtor, and not to determine priorities among adverse claimants. Another requirement might be that the initial creditor/assignor should specifically accept the no-assignment clause in writing. However, this might be impractical in receivables financing, since assignees would have to check carefully each original transaction, in order to ascertain whether the assignor had specifically accepted the no-assignment clause.

23. Another approach might be to provide, as does the UNIDROIT Factoring Convention, that the assignment is effective notwithstanding any agreement between the assignor and the debtor prohibiting such assignment. Such a rule would facilitate the practice of receivables financing, which would benefit from unrestricted transferability of receivables. Moreover, it might be considered that debtors do not need the additional protection that no-assignment clauses are intended to grant them, since debtors are widely permitted to avail themselves of defences,

including set-offs, against assignees. While keeping track of assignments and avoiding clerical and bookkeeping errors may entail some cost to the debtor, this could be viewed as a normal cost of doing business. It may be noted that, in order to accommodate the needs of States having a strong policy in favour of upholding no-assignment clauses, an exception to the above rule has been included in article 6 of the UNIDROIT Factoring Convention. This provision permits States to make a declaration to the effect that assignments contrary to no-assignment clauses shall have no effects towards the debtor, if, at the time of the conclusion of the original transaction, the debtor has its place of business in the State making the declaration.

2. Bulk assignments

24. Bulk assignments of future receivables are, in some jurisdictions, invalidated as being against public policy, in particular if the future receivables arise from contracts that do not exist at the time of assignment. In such jurisdictions, efforts are made by courts to remove obstacles to receivables financing by recognizing the validity of bulk assignments of future receivables provided that the future receivables are, at the time the receivables come into existence, "determined" or "determinable" as to their basic particulars (e.g., the amount and the identity of the debtor).⁸

25. One possible approach, adopted in article 5 of the UNIDROIT Factoring Convention, would be to provide that bulk assignments of all present and future claims are valid between the assignor and the assignee only, leaving the validity of assignment towards third parties to the applicable national law. Such a rule would have the disadvantage that one and the same bulk assignment may be valid as between the parties to the assignment and invalid towards the debtor and third parties. As a result, the debtor could claim that the assignment was invalid towards it, pay the assignor and thus be released. Similarly, if assignment is valid only between the assignor and the assignee, the creditors of the assignor could attach the receivables on the basis that the assignment was invalid towards them, with the result that the receivables would be effectively lost for the assignee. Another possible approach, widely adopted in national legal systems, would be to recognize in general the validity of bulk assignments of future receivables. Such an approach would facilitate receivables financing. The interests of the debtor would be protected, in as much as the debtor would not be obliged to pay the assignee until it would receive notice of the assignment (as to the interests of third parties, see paragraphs 36-42).

B. Form requirements

26. Legal systems differ widely as to the form required. In some jurisdictions, the assignment has to be in writing, while in other jurisdictions even a purely oral assignment suffices. As a result, one and the same assignment may be considered valid in one country and invalid in another. Another problem is that, even within a single jurisdiction, it may not be easy to ascertain the form requirement for a particular assignment, because there may be different requirements for different types of assignments (e.g., assignments by way of sale and assignments by way of security).

27. It appears that "writing", defined in a liberal fashion, would constitute an appropriate form requirement, since, even in the jurisdictions in which oral assignments are valid, parties tend to put assignment in writing. No other form might be necessary for the validity of the assignment between the parties thereto. In addition to writing, one might require notification of the debtor.

⁸ Hein Kötz, Rights of Third Parties. Third Party Beneficiaries and Assignment, International Encyclopedia of Comparative Law, Vol. VII, Ch. 13 (1992), para. 82.

However, imposing such a requirement might create obstacles to assignment, in particular to non-notification assignment, without providing any additional protection for the debtor, since in any case the debtor, in the absence of notification or knowledge of the assignment, could refuse to pay the assignee.

**C. Effects of assignment between the assignor
and the assignee**

28. The effects of assignment between the assignor and the assignee, as between themselves, are usually governed by their contract of assignment and, as against the debtor, are subordinated to the provisions of the original transaction. In practice, parties to receivables financing tend to be very specific in their dealings as to their rights and obligations. Moreover, under the general principles of contract law, the assignor and the assignee must refrain from any action that could defeat or impair the purpose of the assignment. In the absence of a sufficiently detailed agreement, the matter would be dealt with by statutory rules. Such rules tend to address the extent to which the assignor warrants the existence and enforceability of the receivables and the solvency of the debtor. There appear to be few differences between legal systems on this matter. Generally speaking, an assignor who receives a price for the receivables is deemed to warrant their existence. Such a warranty would not exist if the assignee acquired the receivables without paying a price for them, unless the assignor explicitly undertook a warranty. In addition, the assignor usually does not warrant the solvency of the debtor, unless otherwise expressly agreed.

D. Effects of assignment towards the debtor

29. The primary goal of any rules on assignment may be to strike a balance between, on the one hand, the need to allow parties to mobilize receivables in order to obtain finance and, on the other hand, the need to ensure that the legal position of the debtor, who is not a party to the assignment, is not adversely affected by the change in the identity of the creditor. There are two main issues that arise in this context, namely, the conditions that have to be met for the assignment to produce effects towards the debtor, and the defences that the debtor may raise against the assignee.

30. While an assignment may be valid and binding on the assignor and the assignee, it has no effects on the debtor, unless an additional condition is met. While the debtor's obligation to pay to the assignee depends on the debtor acquiring knowledge of the assignment, legal systems differ as to whether a notice to the debtor is required or whether any other act results in the debtor acquiring knowledge of the assignment. Moreover, legal systems requiring notice differ on the effects of knowledge of the assignment on the part of the debtor in case no notice is given.

31. The requirement of a complete written notice would protect the debtor from ambiguities that might arise without such notice, for example, when the debtor has received some information about the assignment but has no information as to the identity of the assignee or the exact value of the assigned receivables. Matters related to written notice include: whether it would cover modern means of communications, such as fax or electronic data communications; the minimum content of the notice, e.g., reasonable identification of the assigned receivables and the assignee; which party can give notice, the assignor or the assignee, e.g., if the assignee is authorized by the assignor to give notice; whether notice is effective when dispatched, received or actually read by the debtor. Another question that would have to be addressed is the question whether the debtor, who has no formal notice of the assignment but knows of it, could pay the assignor and be discharged.

32. Legal systems differ as to which defences the debtor may raise against the assignee. An approach adopted in some jurisdictions is to allow the debtor to raise against the assignee defences

arising out of the same contract giving rise to the assigned receivables, no matter whether such defences arose before or after assignment or before or after notice thereof. Under an approach adopted in some other jurisdictions the debtor is permitted to raise defences arising from a separate contract between the debtor and the assignor, if those defences accrued before the debtor was notified about the assignment, irrespective of when the receivables become payable. An approach followed in yet other jurisdictions is to allow defences arising from a separate contract between the debtor and the assignor, provided that they involve claims that are due both at the time notification is given and at the time the assigned receivables become due. Yet another more liberal approach followed in some jurisdictions is to allow such defences irrespective of when notification took place or when the assigned receivables arise.

33. Legal systems differ on two other noteworthy issues related to defences of the debtor against the assignee demanding payment of the assigned receivables: the kind of proof the debtor is entitled to request, in case of doubt as to whether an assignment has been concluded; and whether the assignee has to return to the debtor any amount advanced, in case the assignor has not fulfilled its obligations towards the debtor under the original transaction. As to the first issue, a possible approach, adopted in some jurisdictions, is to provide that the debtor may request "reasonable" proof. A possible advantage of this approach is that the term "reasonable" is well known; even in jurisdictions in which that term has no technical legal meaning, it is commonly understood in practice. A possible disadvantage of this approach would be that use of the term "reasonable" would not achieve certainty and predictability, since its meaning would depend on the circumstances in which an assignment was concluded. A different approach would be to require written proof, so as to enhance certainty and predictability. As to the second issue, one approach, adopted in article 10 of the UNIDROIT Factoring Convention, is to provide that the assignee does not have to return any advances that the debtor might have made, unless unjust enrichment or bad faith on the part of the assignee was involved. Unjust enrichment could be involved if the assignee receives payment from the debtor but has not paid the assignor at the time the debtor demands the return of the advances made. The assignee might be in bad faith, if, for example, it pays the assignor for the assigned receivables despite knowing that the assignor has not performed its obligations to the debtor under the original transaction.

34. A number of other questions might arise, with respect to which unification might not be needed or feasible, including: whether the debtor can raise defences arising from separate transactions between the debtor and the assignee, or between the debtor and other assignors which might have assigned their receivables to the same assignee; whether, in case of subsequent assignments, the debtor can raise against the last assignee demanding payment any defences that it might have had against a previous assignee.

35. Defences of the debtor against the assignee create uncertainty as to whether the assignee will be able to collect. For that reason, in practice, waiver-of-defences clauses are often included in the contractual terms of the original transaction. In most jurisdictions, such waiver-of-defences clauses agreed upon at the time of the conclusion of the original transaction are generally upheld in commercial, but not necessarily in consumer, settings.⁹ Some jurisdictions recognize waiver-of-defences clauses agreed upon between the debtor and the assignee after the debtor is notified of the assignment, as long as they involve defences that the debtor knew or ought to have known at the time of the waiver that they were available to him. In other jurisdictions, the debtor's acceptance of the assignment, orally or in writing, may be interpreted as a waiver of all or part of the

⁹ *Ibid.*, para. 99.

defences that the debtor might otherwise have against the assignee, provided that it is clear and beyond any doubt that the debtor accepting the assignment intended to waive its defences.

E. Effects of assignment towards third parties: priorities

36. As assignment is, in most jurisdictions, considered to be a contract between the assignor and the assignee, it produces effects between them. However, assignment is also a means of transferring property, and as such it may have effects towards third parties, such as several conflicting assignees, the assignor's creditors and the trustee in the bankruptcy of the assignor. Legal systems differ on whether the effects of assignment towards third parties arise from the assignment itself or from an additional act, such as notification of the debtor or registration of the assignment. A related issue is the order of priority among several creditors laying a claim on the same receivables. The issue of priority arises mainly if the assigned receivables are the main assets the assignor is left with, in particular in the case of insolvency of the assignor, since otherwise the assignor will be able to satisfy its creditors on the basis of other assets. A conflict of priorities may arise in the following situations: between several assignees, due to multiple assignments of the same receivables because of fraud or an unconscionable act of the assignor; between the assignee and the bankruptcy trustee, who may, for example, seek to invalidate the assignment on the ground that it constitutes a fraudulent transaction; between the assignee and the government as creditor of the assignor for taxes. As priority conflicts with the bankruptcy trustee and the government may involve general policy considerations of a social, economic and political character, they might best be left to the applicable national law or they might be addressed in the context of any possible future unification work on cross-border insolvency. This report will discuss only priority conflicts among several assignees or between the assignee and the assignor's creditors.

37. While the issue of third-party effects and the related issue of priorities is important in the context of some kinds of assignment, it may not be of such crucial importance in the context of other kinds of assignment, including: securitization, in which the risk of the insolvency of the assignor might be reduced by the fact that the assignor is usually a financing institution; forfaiting, in which receivables may be backed by a bank guarantee or a stand-by letter of credit and the assignee, in the case of insolvency of the assignor, might be paid out of the proceeds of the bank guarantee or the letter of credit; and project finance, in which the assignee might obtain a number of securities in addition to future proceeds from the project financed.

38. One approach, adopted in some jurisdictions, is to grant priority to the first assignee on the ground that once the assignor has assigned the receivables it does not own them any longer and therefore it cannot assign them a second time. Under such an approach, the assignor's creditors could not attach the receivables, since from the time of the assignment onwards, the receivables do no longer belong to the assignor. Another, similar approach, adopted recently in a jurisdiction in order to facilitate the assignment of trade receivables in the context of financing transactions, is to grant priority to the assignee that holds a document, signed by the assignor, listing the receivables, according to the date on that document (art. 4 of the so called loi Dailly). Such an approach has the advantage of simplicity and certainty, since in no instance could a subsequent assignee prevail. A difficulty with that approach, however, is that it provides no protection to subsequent assignees or to the assignor's creditors, who might have extended credit to the assignor relying on its receivables as security, and who have no way of knowing whether such receivables have already been assigned.

39. Another approach might be to grant priority to the first assignee to notify the debtor. In case of attachment of the assigned receivables by the assignor's creditors, the assignee would prevail, if

it had notified the debtor before attachment. One justification for such an approach could be that, since title to movables passes as a rule only if possession is granted to the transferee, title to receivables should pass only if notice to the debtor, which may be viewed as the nearest equivalent to taking possession, is given. That rule affords some protection to third parties, such as potential creditors of the assignor, since they are in a position to enquire whether the debtor has received a notice of a previous assignment before extending credit to the assignor. However, the application of such a rule might be impractical in receivables financing, where third parties might have to check with a large number of debtors receiving several notices. In addition, debtors could not be forced to provide information to debtors or be made liable for providing inaccurate or false information.

40. Yet another approach might be to grant priority to the first assignee to register the assignment in a public register. In case of attachment of the assigned receivables, the assignee would prevail, if the date of registration would be earlier than the date of attachment (for a discussion of registration, see paragraphs 43-51). Another approach based on a different type of registration would be to grant priority to the assignee that first had its assignment registered in the commercial books of the assignor. Such a system, however, has certain disadvantages. It might be seen as being unreliable, since it would be based on the assumption that the assignor would properly register all assignments. In case the assignor failed to update its books or made an error in registration or registered a subsequent assignment first, the first assignee would lose its priority and might have no remedy against the assignor if the assignor becomes insolvent. One possible way to alleviate the difficulties arising with regard to this system would be to require the assignor to present its books to the assignee so that the assignee could verify the registration by the assignor or could itself register the assignment. However, the utility of such a system might be doubtful in view of the potential difficulty and the time and the cost involved in registering bulk assignments and obtaining access to registered information.

41. If a substantive-law solution to the problem of priorities could not be found, a private-international-law approach might be considered. One such private-international-law solution could be to provide that the effects of assignment toward third parties and the related issue of priorities would be governed by the law of the State where the assignor had its place of business. This approach presents certain advantages. It provides a single point of reference for the bulk assignment in the context of receivables financing, even though the debtors may be resident in several countries. In addition, the law of the assignor's place of business is ascertainable at the time of the assignment even where the debts have not yet come into existence. Moreover, the choice of this law appears to be appropriate in case there is a requirement for registration of the assignment, since potential assignees are likely to look to the assignor's place of business to see whether it has already assigned its receivables. One possible difficulty with such an approach is that it might not be easy to identify the place of business of the assignor, for example, in case a company was registered in one particular place but operated in other places. Another possible difficulty might be that the priority issue could be characterized as an issue of contract, tort, property, bankruptcy or procedural law, which would complicate the elaboration of a generally acceptable private international law rule.

42. Another possible approach would be to devise a rule combining substantive and private international law elements and providing that the first assignee in time, the first assignee to notify the debtor, or the first assignee to register the assignment in a public register would have priority, depending on the approach followed in the law of the State in which the assignor had its place of business. Such an approach would have the disadvantage of failing to produce uniform results. However, it would, to some degree, enhance certainty and could be acceptable in that it would not alter existing approaches to the issue of priorities.

F. Registration

43. Registration of an assignment could be described as the process of filing information about the assignment at a register administered by a public authority for the purpose of providing evidence of title to the receivables, notice about the assignment to interested third parties, or a method for determining priorities. Registration of assignments or other similar transactions is already practiced in some jurisdictions. In some other jurisdictions, registration is currently under consideration by law reform commissions entrusted with the task of modernizing the law on secured transactions, or is suggested as a plausible solution to the problem of priorities.¹⁰ In jurisdictions in which registration of assignments or similar transactions is not practiced, the general concept of registration is not necessarily new, since other types of transactions or rights are already subject to registration, for example, secured transactions with regard to immovables and transactions involving rights related to ships, aircraft, patents, trademarks and copyrights. It should be noted that registration is also practiced in an international context. For example, the World Intellectual Property Organization (WIPO) serves as a registering authority with regard to trademarks and designs. WIPO functions also as an international centralized data bank with regard to patents, which allows international users to obtain access to information registered at national registers. The utility of registration at an international level has also been recognized within the Study Group of UNIDROIT entrusted with the task of preparing uniform rules on certain international aspects of security interests in mobile equipment.¹¹

44. Beyond assignment of receivables, registration is an important issue arising in the context of other possible future work topics of UNCITRAL. Registration and transfer of rights at an international level is an important issue in the context of the negotiability of rights in goods. The Working Group on Electronic Data Interchange adopted at its twenty-seventh session (New York, 28 February-11 March 1994) a recommendation to the Commission that it should authorize the Working Group to undertake preliminary work on negotiability of rights in goods as soon as it has completed the preparation of the model statutory provisions on the legal aspects of electronic data interchange and related means of data communications.¹² It may also be noted that registration of dematerialized or uncertificated securities, i.e., securities that do not have a tangible form, is an important issue that will be touched upon in a preliminary note on future work which the Secretariat intends to submit to the Commission at a future session. Many of the legal issues arising with regard to registration in those different areas might be identical, irrespective of whether the rights transferred are in goods, receivables, or securities, while other legal issues might be different depending on whether registration of rights in goods, receivables or securities is involved.

45. It appears that a solution based on registration would protect the interests of third parties and provide an objective criterion on the basis of which conflicts of priority could be resolved. Moreover, the cost and time involved in registration might not be prohibitive since registration could be based on a computerized register accessible through modern communication systems. As

¹⁰ John Duley, A National Register of Personal Property Securities (Australian Law Reform Commission, Personal Property Securities Research Paper 1); Lane H. Blumenfeld, A hole in the bucket. The unavailability of financial credit due to the lack of a registry in Russian collateral law, Law in Transition (Winter/Spring 1994), p. 14.

¹¹ See UNIDROIT 1993, Study LXXII - Doc. 7 para. 11.

¹² A/CN.9/390, paras. 154-158.

to the issue of privacy of the assignor, which might be of importance for its image in the market, it should be noted that there could be ways to ensure that access to registered information would be available only under certain conditions and only to parties towards whom registration could produce effects (see para. 48). In this context, it should also be noted that financial data of companies, such as assets, encumbrances on assets, loans payments, defaults in payments, dishonored checks, are, in many jurisdictions, already collected by central or commercial banks or other institutions and made available to financing institutions through a national or international telecommunications system. With regard to the concern that even a restricted publicity requirement might unduly interfere with the privacy of the assignor, it may be noted that the possible negative impact of a registration system on the privacy of the assignor would have to be weighed against the potential benefit of the increased chances for obtaining credit on the basis of receivables in an amount closer to their face value.

46. Registration could take place in an international register or in a central national register accessible through an international centralized data bank. An international register would facilitate both registration and access to registered information. Moreover, the legal framework for such an international register would require a set of uniform rules that in all likelihood would need to be in the form of a convention. As to the concerns related to cost of establishment and operation of an international register, simplicity and ease of registration and access to information registered in an international register, a way to alleviate those concerns, at least in part, might be to establish an international registration system with a United Nations agency as registering authority, which would make use of existing means and would be accessible throughout the world due to the universal nature of the United Nations. In case the establishment of an international register proves to be not feasible, a central international data bank might be established so that the information filed at national registers could be made available to international users through modern means of communications. Such a registration system would not necessarily make registration easier for international creditors but it could facilitate their access to the registered information. Central national registration accessible through an international centralized data bank could have the advantage that its implementation might be easier and less costly, since it could benefit from existing national registers and data bases, which, with some modifications, could be integrated into a new registration system. However, such a registration system would to some extent fail to produce uniform results; registration and its effects on third parties would be subject to national law, while issues related to access to registered information could be addressed either in a convention or in a model law. Whether an international register or an international centralized data bank is preferred, the example of WIPO serving as an international registering authority with regard to trademarks and designs and as an international centralized data bank with regard to patents could serve as a precedent (see paragraph 43).

47. Registration raises a number of legal issues, such as its legal effects, authentication of the document to be filed, liability of the registering authority for failing to follow authentication procedures or for errors in the record to be issued by the registering authority upon demand by interested parties, evidential weight of that record, and registration of a statement of release of the assignor in case of assignment by way of security.

48. Registration could be deemed to have a number of legal effects, including: evidence of title or other rights in receivables; notice to third parties about the assignment; and determination of priority among several adverse claimants. One issue that would have to be considered would be whether notice could produce effects against all third parties or against only some categories of third parties, e.g., third parties that could reasonably be expected to search in a register. Financing institutions, for example, that provide credit on the basis of receivables in the ordinary course of their business could reasonably be expected to search in a register. However, for

medium-size or small suppliers of materials on credit, who retain the title on the materials until they are fully paid and obtain rights in the receivables arising from the resale of the end-product as assignees, it might be impracticable to search in registers. Another issue that would arise in case registration were to function as a system to settle priorities would be whether the first assignee to register would be deemed to have priority over assignees that failed to register or registered subsequently, and over creditors of the assignor that attempted to attach the assigned receivables after registration. Were such a rule to be adopted, some exceptions would need to be made.

49. The document to be filed, i.e., the contract of assignment in its entirety or a summary statement thereof, would need to be authenticated. Authentication would be necessary in order to confirm, in particular, whether the assignor and the assignee mentioned in the document filed are the actual parties to the assignment and approve the contents of the document filed. One issue arising in respect to authentication is the authentication procedure that the registering authority would have to follow, e.g., an agreed authentication method, or in the absence of agreement, a reasonable or any authentication method. Another related issue is the liability of the registering authority for failing to follow any authentication method with the result that inaccurate or false information is filed and damage is caused to the parties involved. Yet another issue is the liability of parties entitled to register for filing inaccurate or false information. Provision might have to be made to the effect that the assignee filing an inaccurate or false notice could not benefit from it, and that such an assignee should be liable in damages to the assignor, in case the latter suffers loss as a result of the misconduct. The allocation of responsibility for inaccurate or false filings would presumably have to be different if registration were a joint act of the assignor and the assignee.

50. Upon demand by parties entitled to obtain access to information filed, the registering authority would have to issue a record reflecting the information filed. Such a record might be needed by the assignor or its potential creditors seeking to establish the "creditworthiness" of the assignor on the basis of its receivables. An important issue is the evidential weight of such a record, in particular if it is in the form of a fax or an electronic communication. A related question is the possible liability of the registering authority for errors in such a record, resulting in disparities between the information in the register and the information reflected on the record issued. The responsibility of the registering authority might be limited to direct damages caused by gross negligence and wilful conduct or be expanded to include profits lost as a result of errors in the record issued due to negligence. In this context, provision might have to be made for a mechanism for the payment of claims based on errors of the registering authority. For example, part of the registration fees or other income of the registering authority could be deposited in a fund, and claims against the registering authority could be paid out of the fund.

51. In case of an assignment by way of security in which the assignor fulfilled its obligations under the underlying credit transaction or provided other security, a statement of release of the assignor would have to be filed, whereby the interest of the assignee in the receivables would be waived. Such a statement could be filed by the assignee on its own initiative or upon written demand by the assignor. In case the assignee fails to file such a statement of release in a timely fashion, the assignor may not be able to utilize its receivables for obtaining further credit. In this regard, the issue of the remedies of the assignor arises. One possible remedy is to establish a right of the assignor to request and obtain upon presentation of certain documents a statement of release from the registering authority. Such an approach might be disadvantageous in that it would place an undue burden on the registering authority to check the substance of the documents submitted. Moreover, it could expose the registering authority to liability for errors in the evaluation of the documents. Another possible remedy is to give to the assignor the right to obtain interim relief in the form of an order to the registering authority to issue, or to the assignee to file, a statement of release.

CONCLUSION

52. On the basis of the above discussion, it may be concluded that the disparity of laws on assignment adversely affects the availability and functioning of receivables financing on the international plane. It may further be concluded that the situation could be improved by the preparation of a uniform legal text that would take into account the UNIDROIT Factoring Convention but would go far beyond it, especially as regards its scope of application.

53. As discussed in paragraphs 11 to 16, the scope could be extended to include not only those factoring situations not covered by the UNIDROIT Factoring Convention but also many other transactions encountered in such financial contexts as securitization, project finance and forfaiting of non-documentary receivables. A definite decision on whether assignments of receivables in each of these contexts should be covered requires, it is suggested, a further study which would discuss in respect of these various financial contexts the other questions of scope mentioned in part I (paragraphs 3-10, 17-19) and, in considerable detail and possibly accompanied by some first draft rules, the various substantive issues identified and discussed in part II.

54. Of all the substantive issues addressed in part II, the effects of assignments on third parties, with the related question of priorities, is probably the most complex and difficult one. As may be concluded from the discussion in paragraphs 36 to 51, the feasibility of tackling that issue in an appropriate, universally acceptable manner may be viewed as depending, at least in part, on the feasibility of establishing a reliable registration system. Since such a registration system might be useful also in areas other than receivables (e.g. documents of title, security interests, securities), it is suggested that a separate study be undertaken which would discuss in detail the relevant points, especially the legal aspects of the establishment and operation of a central international register.

55. Yet another conclusion that may be drawn from the discussion in this report is the desirability of the closest possible co-operation with UNIDROIT. Indeed, all possible means of co-operation, including hitherto untried ones, should be explored. For each stage of the preparatory work the most appropriate one should be selected, depending on UNIDROIT's attitude towards the suggested project and on its own work in related areas.

56. If the Commission were to share the above conclusions, it may wish to request the Secretariat to prepare the two studies mentioned in paragraphs 53 and 54. On the basis of those studies, it might wish to decide about the further course of action in this project, in particular whether at that stage a working group should be entrusted with the elaboration of a uniform legal text on receivables financing.

* * *